APPENDIX A

Extract from

"Report and Order on Further Hearing Recommended by Charles A. Webb, Commissioner" served December 22, 1966, in I.C.C. Finance Docket 21510 (pp. 23-28).

C. The Relationship of These Proceedings to the Penn-Central Case

Neither this case nor the *Penn-Central* case can be fully understood if consideration of one is divorced from the other. Unfortunately, the Commission's action in deciding the cases separately has tended to blur vital issues common to both proceedings.

EL, D&H, and B&M cannot survive as independent carriers when the Penn-Central merger is fully consummated. Recognizing that undisputed fact, and not wishing to oppose the rail merger movement in the East, EL, D&H, and B&M filed petitions for inclusion in the Penn-Central system long before the Commission's approval of the N&W-Nickel Plate-Wabash unification. They recognized, however, that affiliation with N&W was more logical and desirable than a union with Penn-Central in that rail competition for much of the traffic moving to and from New England and most of New York State would be preserved. The Commission was moved by the same public interest considerations when it provided in the *Penn-Central* case that the petitions for inclusion in N&W should be determined first; that stockholder rejection of terms of inclusion prescribed by the Commission would bar inclusion in Penn-Central; and that if the petitions for inclusion in N&W were denied, their petitions for inclusion in Penn-Central would be determined.

N&W states in the first sentence of its brief that the reopening of these proceedings is the direct result of the efforts of EL, D&H, and B&M "to protect themselves from the damage that will be inflicted on them by the Penn-Central merger." As an explanation of petitioners' motives, the statement is incomplete. EL, D&H, and B&M, like the New Haven, could have sought inclusion only in the Penn-Central system and, in view of the fact that the value of their properties and the essential services they render would be impaired or destroyed by that merger, with good reason to believe that the Commission would grant their petitions. Whatever problems a Penn-Central merger may pose for N&W, C&O-B&O, WM, Reading and CNJ, the problems of EL, D&H, and B&M could be solved as readily by including them in the Penn-Central system as by including them in the N&W system. Their value to Penn-Central probably would be greater than their value to N&W in view of the anti-competitive aspects of a PRR-NYC-NH-EL-D&H-B&M unification. Obviously, the value of EL, D&H, and B&M to Penn-Central would not be discounted to reflect the traffic diversion potential of the Penn-Central system.

Recognizing that EL, D&H, and B&M perform essential rail transportation services, the Commission attached novel and stringent conditions to its approval of the Penn-Central merger. Specifically, the Commission imposed (1) special traffic conditions designed to prevent any diversion of EL, D&H, and B&M traffic during the pendency of their petitions for inclusion in N&W or in the Penn-Central system;[19] (2) conditions to indemnify EL, D&H, and B&M for any loss of traffic that might occur during the pendency

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[19] 327 I.C.C. at 561-3 (Appendix G, other than paragraphs 3 and 5C thereof relating exclusively to temporary indemnification.)

of said petitions for inclusion;[20] and (3) a condition providing for Commission determination of whether or not a form of capital loss indemnification of the type suggested by EL, D&H, B&M, and N&W should be required.[21]

The matters identified in the preceding paragraph as Items (1), (2), and (3) were set for further hearing in the *Penn-Central* case.[22] The Commission's ultimate decision on Items (1) and (2) should not affect the outcome of these proceedings. The temporary traffic and indemnity conditions under consideration relate essentially to maintenance of the *status quo* pending final determination of the petitions for inclusion, whereas these proceedings are concerned with the burdens and benefits resulting from inclusion. In fact, if EL, D&H, and B&M are included in the N&W system without undue delay, the issues involved in Items (1) and (2) would be rendered largely if not entirely moot.

The temporary indemnification matter (Item (2)) is not factually related to the matter of capital loss indemnification (Item (3)). The former concerns diversion of traffic from

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[20] 327 I.C.C. at 532-4 and 561-3 (Appendix G, paragraphs 3, 5C, and related provisions.)

[21] 328 I.C.C. at 328-9. The term "capital loss," as used by N&W, EL, D&H and B&M in their petitions for reconsideration in the *Penn-Central* case, refers to losses of EL, D&H, and B&M traffic to Penn-Central to the extent not offset by traffic gains attributable to their inclusion in the N&W system, with the net annual loss of income, if any, capitalized at an appropriate rate.

[22] Pursuant to the Commission's Order of September 29, 1966, further hearings commenced on October 31, 1966, under an expedited procedure and with instructions that the capital loss indemnification matter (Item (3)) be heard first "in order that the Commission, if it so desires, may determine that matter prior to its determination of the matters set forth above in Items (1) and (2)." Hearings were concluded on December 16, 1966.

EL, D&H, and B&M as independent carriers, whereas the latter concerns diversion of traffic from EL, D&H, and B&M as components of N&W and not offset by traffic gains resulting from their inclusion.

For obvious reasons, the Commission in its *Penn-Central* reports could not prejudge issues that might arise in further proceedings involving petitions for inclusion in the Penn-Central system. For that reason, and in view of the possibility that unforeseen transportation circumstances might exist at the time of filing petitions for inclusion in the Penn-Central system, the Commission in its Report on Reconsideration was obliged to reject proposals of EL, D&H, and B&M "that would automatically find the latter inclusion [in Penn-Central] consistent with the public interest in the event inclusion in N&W is denied." (328 I.C.C. at 332). Any such act of prejudgment "would render a binding decision in either the *N&W* merger case or in this case extremely difficult and could only lead to further litigation by other carriers which could be adversely affected." (328 I.C.C. at 322).

Necessarily implied in the prior report in this proceeding and in the reports in the *Penn-Central* case is the conclusion that EL, D&H, and B&M, in all probability, will be included either in the existing N&W system or in the Penn-Central system. No other conclusion seems possible in the light of the following facts:

1. The temporary traffic and indemnity conditions for the protection of EL, D&H, and B&M cannot be made permanent under the Commission's general reservation of jurisdiction in the *Penn-Central* case (327 I.C.C. App. I, par. 6). Such action would deny to Penn-Central and to numerous shippers a substantial portion of the benefits justifying approval of the merger.

2. If the services of EL, D&H, and B&M are so important as to justify delay in the consummation of the Penn-Central merger in the absence of novel protective conditions,[23] the continuation of such services after consummation and the expiration of those conditions must have been assumed. For example, the Commission concluded in its initial report in the *Penn-Central* case (327 I.C.C. at 529):

> "The service the three petitioners render their shippers is essential and the public interest dictates that it be preserved. Unless somehow protected, through inclusion herein or by some other equitable means, the petitioners would be adversely affected by the proposed merger to a serious degree and would be severely handicapped in providing required transportation to the highly industralized areas they serve. Though this be true, we shall not require their inclusion in the PRR-NYC merger at this time. They have an established right to obtain first a determination on their petitions for inclusion in the N&W system."

3. If the bankruptcy of three important railroads was considered to be a possible consequence of the Penn-Central merger, the Commission would have so stated, but the Commission's reports in the *Penn-Central* case contain no discussion to the effect that the merger would be consistent with the public interest even if it drove EL, D&H, and B&M into bankruptcy. On the other hand, the *Penn-Central* reports indicate that the merger would be consistent with the public

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[23] The Commisson stated: "It is doubtful that, without inclusion in a major system, these three carriers could withstand the competition of the applicants merged, and, unless they are protected during the period necessary to determine their future, we would not authorize consummation at this time, even though approving the merger." (327 I.C.C. at 532).

interest notwithstanding any lessening of intramodal competition resulting from inclusion of EL, D&H, and B&M.[24]

4. The prior report in these proceedings clearly recognized that inclusion of EL, and hence D&H and B&M, in the N&W system was a mere possibility, not a certainty. The district court in the *Penn-Central* case felt that "no great clairvoyance is needed to predict the likelihood of its [the Commission] finding that the public interest is consistent with inclusion of the three roads on proper conditions in the N&W system . . ." (opinion, note 4), but, as clearly shown by the prior report in these proceedings (324 I.C.C. at 25-26), the existence of "proper conditions" was not regarded as certain.

5. Therefore, the Commission must have determined in the *Penn-Central* case, by necessary implication, that in the absence of stockholder rejection of Commission terms, EL, D&H, and B&M, barring some totally unforeseen development, probably will be included either in the N&W system or in the Penn-Central system.

If the inclusion of EL, D&H, and B&M in either the N&W system or the Penn-Central system is practically assured, their inclusion in the system chosen by the Commission in

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[24] The Commission recognized that the Penn-Central merger would eliminate rail competition in particular areas but viewed the competitive aspects of the merger in the light of a rail transportation market extending from Boston and Norfolk on the east to Chicago and St. Louis on the west. (327 I.C.C. at 507-514). Elimination of rail competition throughout a large part of Florida was not considered a bar to approval of the Seaboard-Coast Line merger. *Seaboard Air Line R. Co.* v. *United States*, 382 U.S. 154 (1965). Elimination of rail competition east of Buffalo in the territory served by EL, D&H, and B&M would be less substantial considering the much larger area embraced by the Penn-Central application.

the furtherance of national transportation objectives should not be on terms which reflect any diminution of capital value attributable to the traffic diversion impact of the other system. In other words, the petitioners should not be penalized for anticipating the Commission's desire to preserve rail competition in the territory they serve. Whether or not the Commission should require capital loss indemnification to facilitate inclusion of petitioners in N&W is a matter which, presumably, will be determined in the light of further hearings in the *Penn-Central* case if such a determination seems necessary or desirable.